Statement of Financial Accounting Concepts No. 6

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Elements of Financial Statements

a replacement of FASB Concepts Statement No. 3 (incorporating an amendment of FASB Concepts Statement No. 2)

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comprehensive income. Thus, this Statement continues unchanged the elements defined in Concepts Statement 3, although it contains added explanations stemming from characteristics of not-for-profit organizations and their operations. It also defines three classes of net assets of not-for-profit organizations, distinguished by the presence or absence of donor-imposed restrictions, and the changes in those classes during a period—change in permanently restricted, temporarily restricted, and unrestricted net assets.

Other Possible Elements of Financial Statements

3. Although the elements defined in this Statement include basic elements and are probably those most commonly identified as elements of financial statements, they are not the only elements of financial statements. The elements defined in this Statement are a related group with a particular focus—on assets, liabilities, equity, and other elements directly related to measuring performance and status of an entity. Information about an entity's performance and status provided by accrual accounting is the primary focus of financial reporting (FASB Concepts Statement No. 1, *Objectives of Financial Reporting by Business Enterprises*, paragraphs 40-48, and FASB Concepts Statement No. 4, *Objectives of Financial Reporting by Nonbusiness Organizations*, paragraphs 38-53). Other statements or focuses may require other elements.[3]

4. Variations of possible statements showing the effects on assets and liabilities of transactions or other events and circumstances during a period are almost limitless, and all of them have classes of items that may be called elements of financial statements. For example, a statement showing funds flows or cash flows during a period may include categories for funds or cash provided by (a) operations, (b) borrowing, (c) issuing equity securities, (d) sale of assets, and so forth. Other projects may define additional elements of financial statements as needed.

Elements and Financial Representations

5. Elements of financial statements are the building blocks with which financial statements are constructed—the classes of items that financial statements comprise. *Elements* refers to broad classes, such as assets, liabilities, revenues, and expenses. Particular economic things and events, such as cash on hand or selling merchandise, that may meet the definitions of elements are not elements as the term is used in this Statement. Rather, they are called *items* or other descriptive names. This Statement focuses on the broad classes and their characteristics instead of defining particular assets, liabilities, or other items. Although notes to financial statements are described in some authoritative pronouncements as an integral part of financial statements, they are not elements. They serve different functions, including amplifying or complementing information about items in financial statements.[4]

6. The items that are formally incorporated in financial statements are financial representations (depictions in words and numbers) of certain resources of an entity, claims to those resources, and the effects of transactions and other events and circumstances that result in changes in those resources and claims. That is, symbols (words and numbers) in financial statements stand for cash in a bank, buildings, wages due, sales, use of labor, earthquake damage

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financial statement concepts

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PURPOSE AND SCOPE

The purpose of this Section is to describe the concepts underlying the development and use of accounting principles in general purpose financial statements (hereafter referred to as financial statements). Such financial statements are designed to meet the common information needs of external users of financial information about an entity. GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section 1100, establishes standards for financial reporting in accordance with generally accepted accounting principles. It describes what constitutes Canadian generally accepted accounting principles and their sources. .01

The Committee expects this Section to be used by preparers of financial statements and accounting practitioners in exercising their professional judgment as to the application of generally accepted accounting principles and in establishing accounting policies in areas in which accounting principles are developing. .02

This Section does not establish standards for particular measurement or disclosure issues. Nothing in the Section overrides any specific Recommendation in another Section of the Handbook or any other accounting principle considered to be generally accepted. Any inconsistency between this Section and another Section will be reviewed by the Committee when that other Section is re-examined. .03

Financial statements

Financial statements of profit oriented enterprises normally include a balance sheet, income statement, statement of retained earnings and cash flow statement. Financial statements of not-for-profit organizations normally include a statement of financial position, a statement of operations, a statement of changes in net assets and a statement of cash flows. Notes to financial statements and supporting schedules to which the financial statements are cross-referenced are an integral part of such statements. .04

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It enables users to identify similarities in and differences between the information provided by two sets of financial statements. Comparability is important when comparing the financial statements of two different entities and when comparing the financial statements of the same entity over two periods or at two different points in time.

.23 Comparability in the financial statements of an entity is enhanced when the same accounting policies are used consistently from period to period. Consistency helps prevent misconceptions that might result from the application of different accounting policies in different periods. When a change in accounting policy is deemed to be appropriate, disclosure of the effects of the change may be necessary to maintain comparability.

Qualitative characteristics trade-off

.24 In practice, a trade-off between qualitative characteristics is often necessary, particularly between relevance and reliability. For example, there is often a trade-off between the timeliness of producing financial statements and the reliability of the information reported in the statements. Generally, the aim is to achieve an appropriate balance among the characteristics in order to meet the objective of financial statements. The relative importance of the characteristics in different cases is a matter of professional judgment.

ELEMENTS OF FINANCIAL STATEMENTS

.25 Elements of financial statements are the basic categories of items portrayed therein in order to meet the objective of financial statements. There are two types of elements: those that describe the economic resources, obligations and equity/net assets of an entity at a point in time, and those that describe changes in economic resources, obligations and equity/net assets over a period of time. Notes to financial statements, which are useful for the purpose of clarification or further explanation of the items in financial statements, while an integral part of financial statements, are not considered to be an element.

.26 The elements defined herein are the most common categories of items portrayed in financial statements. The existence of other items is not precluded. In practice, a balance sheet may include, as a category of assets or liabilities, items that result from a delay in recognition of revenue, expenses, gains and losses. Criteria for the recognition of items in financial statements are discussed in paragraph 1000.44.

.27 In the case of profit oriented enterprises, net income is the residual amount after expenses and losses are deducted from revenues and gains. Net income generally includes all transactions and events increasing or decreasing the equity of the profit oriented enterprise except those that result from equity contributions and distributions. Investors, creditors and other users frequently use net income as a measure of economic performance of profit oriented enterprises.

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In the case of not-for-profit organizations, the excess or deficiency of revenues and gains over expenses and losses is an important indicator to users of the extent to which a not-for-profit organization has been able to obtain resources to cover the cost of its services. .28

Assets

Assets are economic resources controlled by an entity as a result of past transactions or events and from which future economic benefits may be obtained. .29

Assets have three essential characteristics: .30

(a) they embody a future benefit that involves a capacity, singly or in combination with other assets, in the case of profit oriented enterprises, to contribute directly or indirectly to future net cash flows, and, in the case of not-for-profit organizations, to provide services;

(b) the entity can control access to the benefit; and

(c) the transaction or event giving rise to the entity's right to, or control of, the benefit has already occurred.

It is not essential for control of access to the benefit to be legally enforceable for a resource to be an asset, provided the entity can control its use by other means. .31

Liabilities

Liabilities are obligations of an entity arising from past transactions or events, the settlement of which may result in the transfer or use of assets, provision of services or other yielding of economic benefits in the future. .32

Liabilities have three essential characteristics: .33

(a) they embody a duty or responsibility to others that entails settlement by future transfer or use of assets, provision of services or other yielding of economic benefits, at a specified or determinable date, on occurrence of a specified event, or on demand;

(b) the duty or responsibility obligates the entity leaving it little or no discretion to avoid it; and

(c) the transaction or event obligating the entity has already occurred.

Liabilities do not have to be legally enforceable provided that they otherwise meet the definition of liabilities; they can be based on equitable or constructive obligations. An equitable obligation is a duty based on ethical or moral considerations. A constructive obligation is one that can be inferred from the facts in a particular situation as opposed to a contractually based obligation. .34

Equity/Net assets

Equity is the ownership interest in the assets of a profit oriented enterprise after deducting its liabilities. While equity of a profit oriented enterprise in total is a residual, it includes specific categories of .35

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items, for example, types of share capital, contributed surplus and retained earnings.

.36 In the case of a not-for-profit organization, net assets, sometimes referred to as equity or fund balances, is the residual interest in its assets after deducting its liabilities. Net assets may include specific categories of items that may be either restricted or unrestricted as to their use.

Revenues

.37 Revenues are increases in economic resources, either by way of inflows or enhancements of assets or reductions of liabilities, resulting from the ordinary activities of an entity. Revenues of entities normally arise from the sale of goods, the rendering of services or the use by others of entity resources yielding rent, interest, royalties or dividends. In addition, many not-for-profit organizations receive a significant proportion of their revenues from donations, government grants and other contributions.

Expenses

.38 Expenses are decreases in economic resources, either by way of outflows or reductions of assets or incurrences of liabilities, resulting from an entity's ordinary revenue generating or service delivery activities.

Gains

.39 Gains are increases in equity/net assets from peripheral or incidental transactions and events affecting an entity and from all other transactions, events and circumstances affecting the entity except those that result from revenues or equity/net assets contributions.

Losses

.40 Losses are decreases in equity/net assets from peripheral or incidental transactions and events affecting an entity and from all other transactions, events and circumstances affecting the entity except those that result from expenses or distributions of equity/net assets.

RECOGNITION CRITERIA

.41 Recognition is the process of including an item in the financial statements of an entity. Recognition consists of the addition of the amount involved into statement totals together with a narrative description of the item (e.g., "inventory", "sales", or "donations") in a statement. Similar items may be grouped together in the financial statements for the purpose of presentation.

.42 Recognition means inclusion of an item within one or more individual statements and does not mean disclosure in the notes to the financial statements. Notes either provide further details about items recognized in the financial statements, or provide information about items

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